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In the Supreme Court of the United States

OCTOBER TERM, 1929

ROBERT H. LUCAS, COMMISSIONER OF INTERNAL REVENUE, PETITIONER

v.

NATIONAL INDUSTRIAL ALCOHOL COMPANY, INC.

PETITION FOR A WRIT OF CERTIORARI TO THE COURT OF APPEALS OF THE DISTRICT OF COLUMBIA AND BRIEF IN SUPPORT THEREOF

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v.

NATIONAL INDUSTRIAL ALCOHOL COMPANY, INC.

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PETITION

The Solicitor General on behalf of the Commissioner of Internal Revenue prays that a writ of certiorari issue to review the judgment of the Court of Appeals of the District of Columbia rendered in the above-entitled cause (R. 39, 44), reversing in part the decision of the United States Board of Tax Appeals.

STATEMENT

This case reached the Court of Appeals of the District of Columbia, on the petition of the National Industrial Alcohol Company, respondent,

for a review of the decision of the United States Board of Tax Appeals determining deficiencies in respondent's income and profits taxes for the fiscal years ended May 31, 1919, and May 31, 1920.

The material facts are not in dispute, and may be briefly stated as follows (R. 11):

The respondent, a Louisiana corporation, organized in 1911, and having its principal office in New Orleans, Louisiana, was engaged in the brewery business. On November 3, 1919, respondent abandoned the manufacture of beer and entered upon the cereal beverage business. This business was discontinued in 1923.

For the manufacture of beer, respondent used two brick buildings, separated by a driveway. Each building was three stories high and of the same dimensions, 100 feet by 50 feet. The walls of the brewery building were two feet thick, and the walls of the so-called cellar building were four feet thick and insulated with cork. The foundation of this building was also heavier than that of the brewery building. The cellar building only contained refrigeration pipes. The depreciated cost of the two buildings and additions as of May 31, 1918, was $124,119.09. They were constructed as a complete unit. After prohibition went into effect, the brewery building and one floor only of the cellar building were used for manufacturing the cereal beverage. Two floors of the cellar building, and fifty-eight large vats therein contained, were

not used after November 3, 1919. The vats were either constructed of such material or so constructed as to render their removal impossible or impracticable.

The Commissioner of Internal Revenue disallowed deductions claimed by the respondent for losses due to the abandonment of the beer vats and the two floors of the cellar building. The respondent appealed to the United States Board of Tax Appeals, which affirmed the Commissioner's action with the exception of his disallowance of the depreciated value of the abandoned vats, which the Board held was deductible on account of obsolescence over the period from November 18, 1917, to January 16, 1920, the date which the Board found to be the date on which it became certain these vats could not again be used by the respondent. (R. 14.) The respondent filed its petition for a review of the decision of the Board of Tax Appeals, electing to stipulate with counsel for the Commissioner of Internal Revenue that, pursuant to Section 1002 (d) of the Revenue Act of 1926, c. 27, 44 Stat. 9, 110 (U. S. C. App., Title 26, Sec. 1225), the review might be had in the Court of Appeals of the District of Columbia. (R. 16, 17.)

On February 4, 1930, the Court of Appeals of the District of Columbia rendered its decision (R. 35) reversing the Board's decision with respect to the losses claimed by respondent to be due to the abandonment of the two floors of the cellar building.

Timely motion for rehearing and modification of this judgment was filed by the petitioner herein on February 18, 1930 (R. 39), and denied by the court on March 1, 1930 (R. 44). On the same day the court issued its mandate to the Board of Tax Appeals directing a recomputation of the tax in accordance with its opinion. Petitioner herein moved the court to recall its mandate. This motion was denied on March 8, 1930. (R. 45.)

SPECIFICATION OF ERROR TO BE URGED

The court below erred in holding that, where tangible assets are abandoned because the business in which they are used is proscribed by prohibition legislation, a taxpayer may deduct from income any amount as a loss of such assets under Section 234 (a) (4) or Section 234 (a) (7) of the Revenue Act of 1918.

REASONS FOR GRANTING THE WRIT

1. The decision in the present case is in conflict with and contrary to the decisions of this Court.

In *Clarke* v. *Haberle Crystal Springs Brewing Co.,* 280 U. S. 384, this Court denied the taxpayer the right to deduct any amount from income under the provisions of Section 234 (a) (7) of the Revenue Act of 1918, for "exhaustion, including obsolescence, of its good will," on the ground that when a business is extinguished as noxious under the Constitution the owners can not demand compensation from the Government, or a partial

compensation in the form of an abatement of taxes otherwise due. This ruling is equally applicable to loss in the value of tangible property caused by the enforced abandonment of its use in the prohibited business.

In *Renziehausen* v. *Lucas,* 280 U. S. 387, a claim for deductions on account of obsolescence of good will of a distilling business, resulting from prohibition legislation, was denied on the basis of the decision in the *Haberle Brewing Company case.*

2. On April 28, 1930, this Court, on the petition of the Commissioner of Internal Revenue, granted its writ of certiorari to review the decision of the United States Circuit Court of Appeals for the Second Circuit, in the case of *Lucas* v. *Niagara Falls Brewing Co.,* No. 741, October Term, 1929. In that case the Circuit Court of Appeals, relying upon its decision in *Haberle Crystal Springs Brewing Co.* v. *Clarke,* 30 F. (2d) 219, allowed a deduction for obsolescence of tangible property used in a business extinguished by national prohibition. In the case at bar, the respondent claimed the deduction either as obsolescence under Section 234 (a) (7), or as a loss under Section 234 (a) (4). The claim under Section 234 (a) (7) will be disposed of by this Court when the *Niagara Falls Brewing Company case* is reviewed.

3. The question is of present importance in administering the Federal income tax laws since it is involved in cases now pending in the courts, the

Board of Tax Appeals, and the Bureau of Internal Revenue. Without a decision of this Court, the Commissioner of Internal Revenue is unable to determine the proper principle to be applied in such cases, and acceptance of the decision in the present case would leave the matter in confusion. Although the Commissioner believes that this Court has announced in the *Haberle Brewing Company case, supra,* the proper principle to be applied in such cases, whether involving tangible or intangible property, confusion results from the fact that in the cited case the sole question was whether deductions could be allowed for obsolescence of intangible property.

Wherefore, it is respectfully submitted that this petition should be granted.

THOMAS D. THACHER,
Solicitor General.

MAY, 1930.

BRIEF IN SUPPORT OF PETITION

OPINION BELOW

The opinion of the Court of Appeals of the District of Columbia (R. 35) is not yet reported. The findings of fact and opinion of the United States Board of Tax Appeals (R. 11–15) are reported in 7 B. T. A. 1241.

JURISDICTION

The decision of the Court of Appeals of the District of Columbia, reversing the Board of Tax Appeals, was rendered February 4, 1930. (R. 35.) Motion for rehearing, filed February 18, 1930, was denied March 1, 1930. (R. 44.) Jurisdiction is conferred upon this Court by Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

The sole question herein presented is whether the abandonment of tangible property constitutes an allowable deduction as a loss under Section 234 (a) (4) or as obsolescence under Section 234 (a) (7) of the Revenue Act of 1918, c. 18, 40 Stat. 1057, 1077, 1078, when such abandonment is directly attributable to the proscription of the taxpayer's business by virtue of the Eighteenth Amendment to the Constitution of the United States and national legislation enacted pursuant thereto.

STATUTE INVOLVED

Revenue Act of 1918, c. 18, 40 Stat. 1057, 1077, 1078:

> SEC. 234. (a) That in computing the net income of a corporation subject to the tax imposed by section 230 there shall be allowed as deductions:
>
> * * * * *
>
> (4) Losses sustained during the taxable year and not compensated for by insurance or otherwise.
>
> * * * * *
>
> (7) A reasonable allowance for the exhaustion, wear and tear of property used in the trade or business, including a reasonable allowance for obsolescence.
>
> * * * * *

STATEMENT

The facts are sufficiently stated in the petition for certiorari.

ARGUMENT

The court below holds that, since it appears that the respondent herein ceased the manufacture of beer on November 3, 1919, because of national prohibition, and abandoned the use of two floors of its cellar building, the value of those two floors constitutes a loss deductible from gross income, since that portion of the building had no value to respondent from the date of abandonment on November 3, 1919, and the entire value to respondent of those abandoned floors ceased with the outlawing of its brewing business. The authorities relied upon by

the court for this position are the cases of *Dean* v. *Hoffheimer Bros. Co.,* 29 F. (2d) 668, and *United States* v. *White Dental Co.,* 274 U. S. 398. Neither of these cases treats the issue here raised from the viewpoint of the deductibility of a loss resulting from legislative proscription of the taxpayer's business, and both of the cited cases were decided prior to the decisions of this Court in the cases of *Clarke* v. *Haberle Crystal Springs Brewing Co.,* 280 U. S. 384, and *Renziehausen* v. *Lucas,* 280 U. S. 387, in which this Court ruled upon a deduction claimed for obsolescence of intangible property rendered obsolete or obsolescent by prohibition legislation. In the former case this Court said (p. 386):

> * * * when a business is extinguished as noxious under the Constitution the owners can not demand compensation from the Government, or a partial compensation in the form of an abatement of taxes otherwise due.

This principle is equally applicable to deductions claimed because of the abandonment or obsolescence of tangible property used in a business which is extinguished as noxious under the Constitution. It is submitted that the foregoing cases are controlling in the instant case, and that no deductions from gross income representing losses or obsolescence of tangible property arising out of or consequential upon the enactment of national prohibition are lawfully allowable.

It is respectfully submitted that the decision of the Court of Appeals of the District of Columbia is

in conflict with the decisions of this Court, and leaves in grave doubt the proper course to be followed by the Commissioner of Internal Revenue in disposing of pending cases involving the question herein.

CONCLUSION

In order that there may be a conclusive determination of an important principle involved in the administration of the Federal income tax laws, it is urged that this petition be granted.

Respectfully submitted.

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